

RBI/2010-11/497 A. P. (DIR Series) Circular No. 57

May 2, 2011

Pledge of shares for business purposes

Under the extant FEMA regulations, powers have been delegated to the Authorised Dealer Category - I (AD Category - I) banks to convey 'no objection' to the resident eligible borrowers under the extant External Commercial Borrowings (ECB) guidelines for pledge of shares held by the promoters, in accordance with the Foreign Direct Investment (FDI) policy, in the borrowing company / domestic associate company of the borrowing company as security for the ECB, subject to certain conditions [c.f. A. P. (DIR Series) Circular No. 1 dated July 11, 2008]. Pledge of shares in respect of all other FDI related transactions requires the prior permission of the Reserve Bank.

2. The extant FEMA regulations have since been reviewed and it has been decided to further liberalise, rationalise and simplify the processes associated with FDI flows to India and reduce the transaction time. Accordingly, it has been decided to delegate powers to the AD Category - I banks to allow pledge of shares of an Indian company held by non-resident investor/s in accordance with the FDI policy in the following cases subject to compliance with the conditions indicated below:

(i) Shares of an Indian company held by the non-resident investor can be pledged in favour of an Indian bank in India to secure the credit facilities being extended to the resident investee company for bonafide business purposes subject to the following conditions :

- in case of invocation of pledge, transfer of shares should be in accordance with the FDI policy in vogue at the time of creation of pledge;
- submission of a declaration/ annual certificate from the statutory auditor of the investee company that the loan proceeds will be / have been utilized for the declared purpose;
- the Indian company has to follow the relevant SEBI disclosure norms; and

pledge of shares in favour of the lender (bank) would be subject to compliance with the Section 19 of the Banking Regulation Act, 1949.

(ii) Shares of the Indian company held by the non-resident investor can be pledged in favour of an overseas bank to secure the credit facilities being extended to the non-resident investor / non-resident promoter of the Indian company or its overseas group company, subject to the following conditions :

- loan is availed of only from an overseas bank;
- loan is utilized for genuine business purposes overseas and not for any investments either directly or indirectly in India;
- overseas investment should not result in any capital inflow into India;

in case of invocation of pledge, transfer should be in accordance with the FDI policy in vogue at the time of creation of pledge; and

submission of a declaration/ annual certificate from a Chartered Accountant/ Certified Public Accountant of the non-resident borrower that the loan proceeds will be / have been utilized for the declared purpose.

2. Necessary amendments to the Notification No. FEMA 20/2000-RB dated May 3, 2000, are being issued separately.

3. AD Category - I banks may bring the contents of this circular to the notice of their constituents and customers concerned.

4. The directions contained in this circular have been issued under sections 10(4) and 11(1) of the Foreign Exchange Management Act, 1999 (42 of 1999) and are without prejudice to permissions / approvals, if any, required under any other law.

Yours faithfully,

(Meena Hemchandra)
Chief General Manager-in-Charge